IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 121 of 1989

For Approval and Signature:

Hon'ble MR.JUSTICE J.M.PANCHAL
and
Hon'ble MR.JUSTICE M.S.SHAH

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

COMMISSIONER OF INCOME-TAX

Versus

ARUNA MILLS LTD

Appearance:

MR BB NAIK with MR MANISH R BHATT for Petitioner

Notice served for Respondent

CORAM : MR.JUSTICE J.M.PANCHAL
and
MR.JUSTICE M.S.SHAH

Date of decision: 15/02/2001

ORAL JUDGEMENT

(Per : MR.JUSTICE M.S.SHAH)

In this Reference, at the instance of the Revenue, the following questions are referred to us for

our opinion in respect of A.Y. 1980-81 :

(1) Whether, the assessee is entitled to allowance of excise duty liability of Rs. 1,98,472/- for assessment year 1980-81 when the excise authorities had only issued show cause notice and the claim was disputed by the assessee ?

(2) Whether, when no determination was made in respect of the excise liability and demand was raised by show cause notice which were disputed, the claim of allowance made by the assessee was justified ?

2. In respect of A.Y. 1980-81 relevant to accounting year 1979, the assessee, following the mercantile system of accounting, claimed deduction of Rs. 1,98,472 on the ground of excise duty liability on the basis of notice dated 11.2.1980 from the Excise Department. The I.T.O. rejected the claim on the ground that the liability in question was claimed to have arisen only on account of a show-cause notice [under Rule 10(1) of the Central Excise Rules, 1944 (hereinafter to be referred to as the "Rules")] and, therefore, the said liability could not be said to have accrued and arisen during the accounting year ending on 31.12.1979.

The assessee challenged the aforesaid disallowance before the C.I.T.(appeals) who held in favour of the assessee on the ground that the liability to pay excise duty accrued at the time of manufacture of goods and transfer thereof to the weaving department and that since manufacture and transfer of yarn to the weaving department had taken place during the accounting year under consideration, the claim for deduction of additional excise duty from assessable income was admissible.

In the appeal filed by the Revenue, the Income-tax Appellate Tribunal ("the Tribunal" for brevity) confirmed the decision of the C.I.T. (Appeals). The Tribunal held that since the law under which the excise duty was payable by the assessee-Company, was in operation during the accounting year under consideration, the assessee incurred liability to pay excise duty in terms of the operative law as soon as it manufactured the goods and removed them to weaving department. The Tribunal further held that the fact that the assessee did not provide the said liability in its books of account

suo motu and that it did so on the basis of demand notice dated 11.2.1980, would not postpone the accrual of the liability to the date of demand notice. In view of the aforesaid decision of the Tribunal in favour of the assessee, the Revenue has come-up in Reference before us.

3. At the hearing of the Reference, Mr.B.B.Naik, learned counsel for the Revenue has relied on the decisions of the Bombay High Court in (1) STANDARD MILLS CO.LTD. v. COMMISSIONER OF INCOME-TAX, (1998) 229 ITR 366, and (2) COMMISSIONER OF INCOME-TAX v. INDIAN SMELTING AND REFINING CO. LTD. (1998) 230 ITR 194 taking the view that mere issuance of a show-cause notice by the Excise Department does not result into accrual of liability for the assessee to pay excise duty and that it is only upon adjudication that liability crystallizes. Hence, deduction on account of excise duty liability can be claimed only in the year in which adjudication order is made and not in the year in which a mere show-cause notice is issued.

4. Though served, none appears for the respondent.

5. We have looked into the order passed by the Tribunal. Though the judgment of the Tribunal does not disclose consideration of any case law, it appears from the order of the C.I.T.(appeals) confirmed by the Tribunal and the other orders passed by the Tribunal in similar matters that the Tribunal had relied upon the decision of the Calcutta High Court in COMMISSIONER OF INCOME-TAX, CENTRAL, CIRCLE I, CALCUTTA v. CENTURY ENKA LTD. (1981) 130 ITR 267, wherein Mr.Justice Sabyasachi Mukharji (as His Lordship then was) held that in all fiscal statutes, normally, a charge is created which may also be described as a declaration of liability indicating what would be liable to taxation. The second stage is the quantification of that liability in the form of an assessment and the third stage is the recovery. In fiscal statutes, the mischief of taxation is on the happening or occurrence of the taxable event. Thus, the sales tax is a tax on sale and, therefore, the sale of goods attracts the duty. Similarly, under the Central Excises and Salt Act, 1944, the duty is attracted on the production or the manufacture of the goods. The Calcutta High Court then relied on the decision of the Supreme Court in KEDARNATH JUTE MFG. CO.LTD. v. COMMISSIONER OF INCOME-TAX (CENTRAL), CALCUTTA, (1971) 82 ITR 363 which was a case under the sales tax laws. The Supreme Court has held that the sales tax being a tax on sale, the liability to pay sales tax accrues as soon as the sale takes place irrespective of the fact whether the assessee had reflected his liability in its books of

account or whether the demand by Sales Tax Department was disputed by the assessee.

Similarly, the Kerala High Court also took a similar view in EDDY CURRENT CONTROLS (INDIA) LTD. v. COMMISSIONER OF INCOME-TAX, (1992) 198 ITR 491.

6. Before dealing with the controversy on merits, we would like to refer to Rule 10 of the Rules as it was in force till 16th November, 1980, since it was under the said Rule that notice in question was issued. Rule-10 as it stood reads as under :

"10(1) Where any duty has not been levied or paid or has been short levied or erroneously refunded or any duty assessed has not been paid in full, the proper officer may, within six months from the relevant date, serve notice on the person chargeable with the duty which has not been levided or paid, or which has been short levied, or to whom the refund has erroneously been made, or which has not been paid in full, requiring him to show cause why he shouldnot pay th amount specified in the notice :

Provided that -

(a) where any duty has not been levied or paid, has been short levied or has not been paid in full, by reason of fraud, collusion or any wilful mis-statement or suppression of facts by such person or his agent, or

(b) where any person or his agent, contravenes any of the provisions of these rules with intent to evade payment of duty and has not paid the duty in full, or

(c) where any duty has been erroneously refunded by reason of collusion or any wilful misstatement or suppression of facts by such person or his agent, the provisions of this sub-section shall, in any of the cases referred to above, have effect as if for the words "six months", the words "five years" were substituted.

Explanation : where the service of the notice is stayed by an order of court,the period of such stay shall be excluded in computing the period of six months, or five years, as the case may be

(2) The Assistant Collector of Central Excise shall, after, considering the representation, if any made by the person on whom notice is served under su-rule(1) determine the amount of duty due from such person (not being in excess of the amount specified in the notice) and thereupon such person shall pay the amount so determined.

For the purposes of this rule -

(i) 'refund' includes rebate referred to in rules 12 and 12A.

(ii) 'relevant date' means -

(a) in the case of excisable goods on which duty has not been levied or paid or on which duty has been short levied or has not been paid in full, the date on which the duty was required to be paid under these rules;

(b) in the case of excisable goods on which the value or the rate of duty has been provisionally determined under these rules, the date on which the duty is adjusted after final determination of the value of the rate of the duty, as the case may be;

(c) in the case of excisable goods on which duty has been erroneously refunded, the date of such refund."

7. A perusal of the aforesaid rule shows that first the Excise Authority is required to issue a show-cause notice under sub-rule(1) of Rule-10. Where any duty has not been levied or paid or has been short levied or erroneously refunded or any duty assessed has not been paid in full, the assessee is to be given an opportunity to show cause as to why such duty should not be levied or required to be paid. Sub-rule (2) then provides that after considering the representation, if any, made by the assessee, the Assistant Collector of Central Excise, shall determine the amount of duty due from such person and thereupon such person shall pay the amount so determined. Though notices under Rule-10 are sometime loosely referred to as demand notices, it is necessary to make distinction between a show-cause notice under sub-rule(1) and demand notice under sub-rule(2) of Rule-10 of the said Rules. A notice under sub-rule (1) i.e. show-cause notice does not determine liability of the assessee, but it merely gives an opportunity to the

assessee to make representation to the authorities for submitting that the excise duty as tentatively claimed by the Department is not required to be levied or paid by the assessee. On the other hand, the decision under sub-rule(2), whether couched in the form of an order or demand notice is the adjudication order (or order in original as it is often called) determining the liability of the assessee to pay an ascertained amount about which there is nothing uncertain provisional, tentative or contingent.

8. Coming to the facts of the present case, in view of the statement of the case submitted by the Tribunal and the questions referred to us, it is obvious that the notice dated 11.2.1980 from the Excise Department was merely a show-cause notice under sub-rule(1) of Rule-10.

9. Even after analysis of the aforesaid Rule-10, the question would still survive whether the assessee can claim deduction of excise duty payable as per the show-cause notice under sub-rule(1) of Rule 10 on the ground that the liability to pay excise duty had accrued on the date of manufacture of the goods which taxable event took place during the accounting year under consideration. As stated above, the Bombay High Court on the one hand and the Calcutta High Court and the Kerala High Court on the other hand had taken drametrically opposite views. Fortunately for us, this controversy is now concluded by the decision of the Supreme Court in COMMISSIONER OF INCOME-TAX v. BHARAT CARBON AND RIBBON MANUFACTURING CO.P.LTD. (1999) 239 ITR 505, wherein it is held in the context of a somewhat similar controversy that the obligation under the excise duty law to pay excise duty arises at the stage when the department issues demand notice after show-cause notice and that raising of the dispute by the assessee for quashing or deduction of liability fastened by the demand notice, would not be a ground for holding that the liability to pay excise duty as per demand notice was not incurred.

10. In the facts of that case before the Apex Court, the assessee was following the mercantile system of accounting. On March 11, 1980 a notice was issued requiring the assessee to show cause as to why the approval of the classification of carbon paper under relevant entry should not be withdrawn with effect from March 16, 1976. Thereafter, the assessee received a demand letter dated April 21, 1980 in the form of demand notice for payment of excise duty for A.Ys.1976-77, 1978-79 and 1979-80, in all demanding a sum of Rs. 92,98,805/-. The assessee filed a writ petition

challenging levy of excise duty. Pending the writ petition, the assessee filed revised return before the Income-tax Authorities claiming an amount of Rs. 92,98,805/- as deduction. The Income-tax Officer disallowed the claim of the assessee for A.Y. 1980-81 on the ground that only a show-cause notice was issued in the said assessment year. In respect of subsequent A.Y. 1981-82, the claim of the assessee was rejected by the I.T.O. on the ground that as the assessee maintained the mercantile system of accounting, the claim for earlier years was inadmissible. He further observed that liability had arisen in that year, but the same would have been allowed if the liability was in present and not in future; as the dispute was pending in a writ petition it was a contingent liability. In appeal, the C.I.T.allowed the claim of the assessee on the basis of the decision in Kedarnath's case (supra). The Tribunal dismissed the appeal as well as the application under section 256(1) for referring the questions to the High Court. Hence, the Revenue went in appeal before the Supreme Court.

11. In the background of the aforesaid facts, the Apex Court held that liability to pay excise duty had arisen on April 21, 1980, when the Excise Department issued demand notice asking the assessee to pay excise duty for the relevant years being A.Ys. 1976-77, 1978-79 & 1979-80. Since the demand notice was issued on April 21, 1980, the assessee following the mercantile system of accounting, had rightly claimed deduction for the said amount for A.Y. 1981-82. Prior to that assessment year, there was no demand. The obligation to pay excise duty arose in A.Y. 1981-82. The liability had been quantified and the demand therefor had been made under the demand notice dated April 21, 1980. There was nothing uncertain, tentative, provisional or contingent in the matter of the assessee's liability to pay the excise duty and that under the law, the assessee was bound to pay the same till the order directing the assessee to pay the same was set aside or modified. The aforesaid decision has been rendered by the Apex Court after considering its decision in Kedarnath's case (supra). Though it does not expressly make any reference to the decisions of the Bombay High Court in (1) STANDARD MILLS, (1998) 229 ITR 366, and (2) INDIAN SMELTING AND REFINING CO.LTD. (1998) 230 ITR 194, the decision of the Apex Court in Bharat Carbon (supra) confirms the view taken by the Bombay High Court in the aforesaid decisions that the liability to pay excise duty accrues when the Excise Department passes the adjudication order i.e. when the demand notice is issued under sub-rule (2) of

Rule-10 after issuance of show-cause notice under sub-rule (1) of Rule-10.

12. In view of the aforesaid clear pronouncement of the Apex Court and in view of the undisputed fact as stated in the statement of case submitted by the Tribunal that the assessee had claimed deduction of excise duty liability on the basis of show-cause notice dated 11.2.1980 for the accounting year 1979 relevant to A.Y. 1980-81, we are of the view that the Tribunal erred in holding that the assessee was entitled to allowance of excise duty liability of Rs. 1,98,472 for A.Y. 1980-81. We have already expressed the opinion that the liability to pay excise duty would accrue on the date when the department passes adjudication order under sub-rule(2) of Rule 10, if at all any order comes to be passed. Mr. Naik for the Revenue, however, states that such order did not come to be passed as the show-cause notices for claiming excise duty at the sizing stage came to be challenged by the Textile Mills and ultimately the Supreme Court held in favour of the Textile Mills as per the ratio laid down in Para (1) of the judgment in J.K.COTTON MILLS v. UNION OF INDIA, AIR 1988 SC 191

13. In view of the above answer to Question no.1, in our opinion, Question no.2 does not survive, because, the question of any dispute having been raised by the assessee against a show-cause notice issued by the Excise Department is of no significance when the liability to pay excise duty does not accrue till the passing of the adjudication order or order in original under sub-rule-(2) of Rule-10 (as it then stood), which may be treated as or followed by a 'demand notice'.

14. We accordingly answer Question No.1 in the negative i.e. in favour of the Revenue and against the assessee. As far as Question no.2 is concerned, in view of our answer to Question no.1, Question no.2 does not survive.

15. The Reference accordingly stands disposed of with no order as to costs.

(J.M.Panchal,J.) (M.S.Shah,J.)